

Family Settlement Complexities - Commercial, Tax and Regulatory Perspective

WIRC

Direct Tax Refresher Course

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Table of contents

Introduction

Interconnect between Family & Business

Indian Landscape

Key Aspects of a Family Arrangement

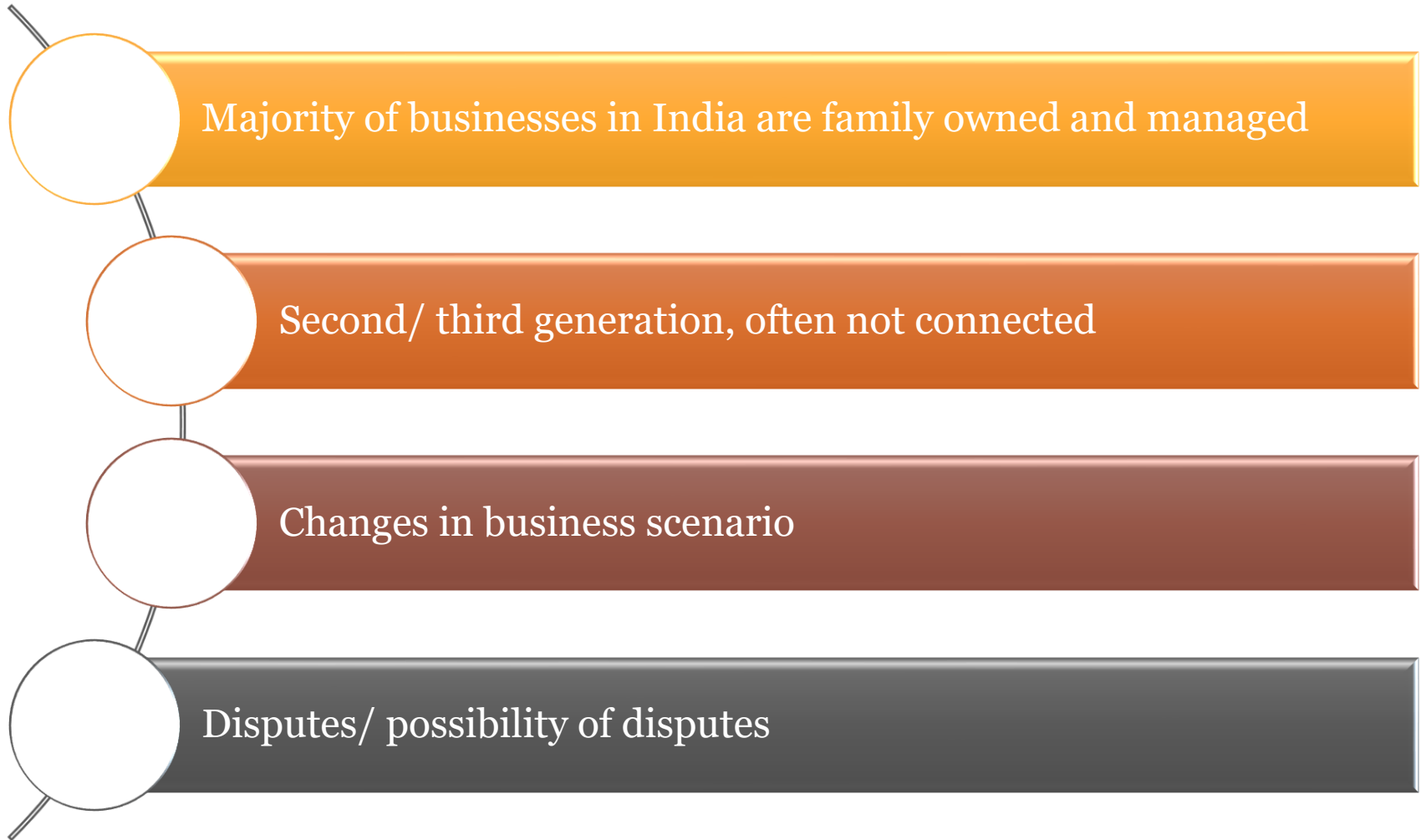
Complexities: CRT Angle

Key Takeaways

Introduction



Introduction

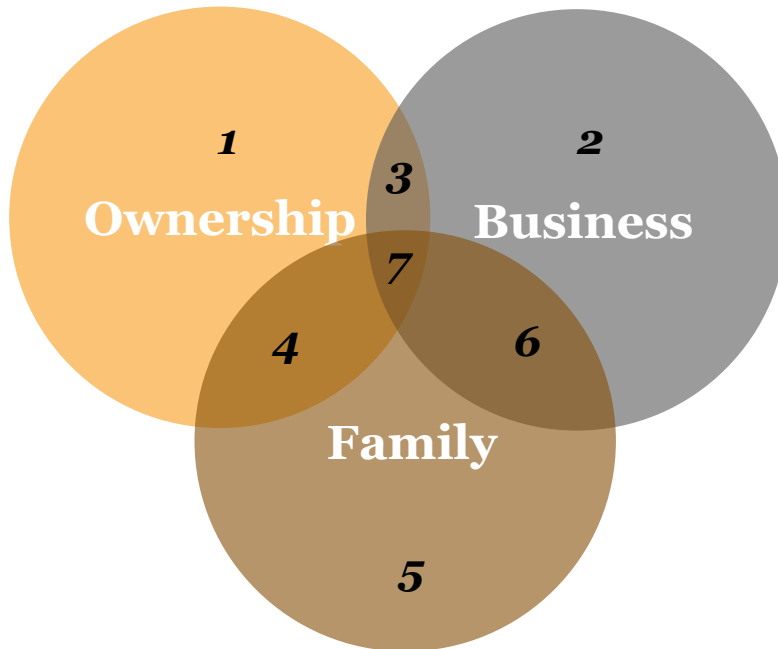


Interconnect between Family and Business

Size of the family and family dynamics

Wealth Complexity: Business and Personal Wealth

Involvement of family members and other professionals in business



Key

1. Inactive or passive owners
2. Management and employees
3. Owner managers
4. Inactive or passive owners/ family members
5. Family
6. Family employees
7. Working family owners

Indian Landscape – A few examples



**Reliance
Group**



**OP Jindal
Group**



Hero Group



Bajaj Group

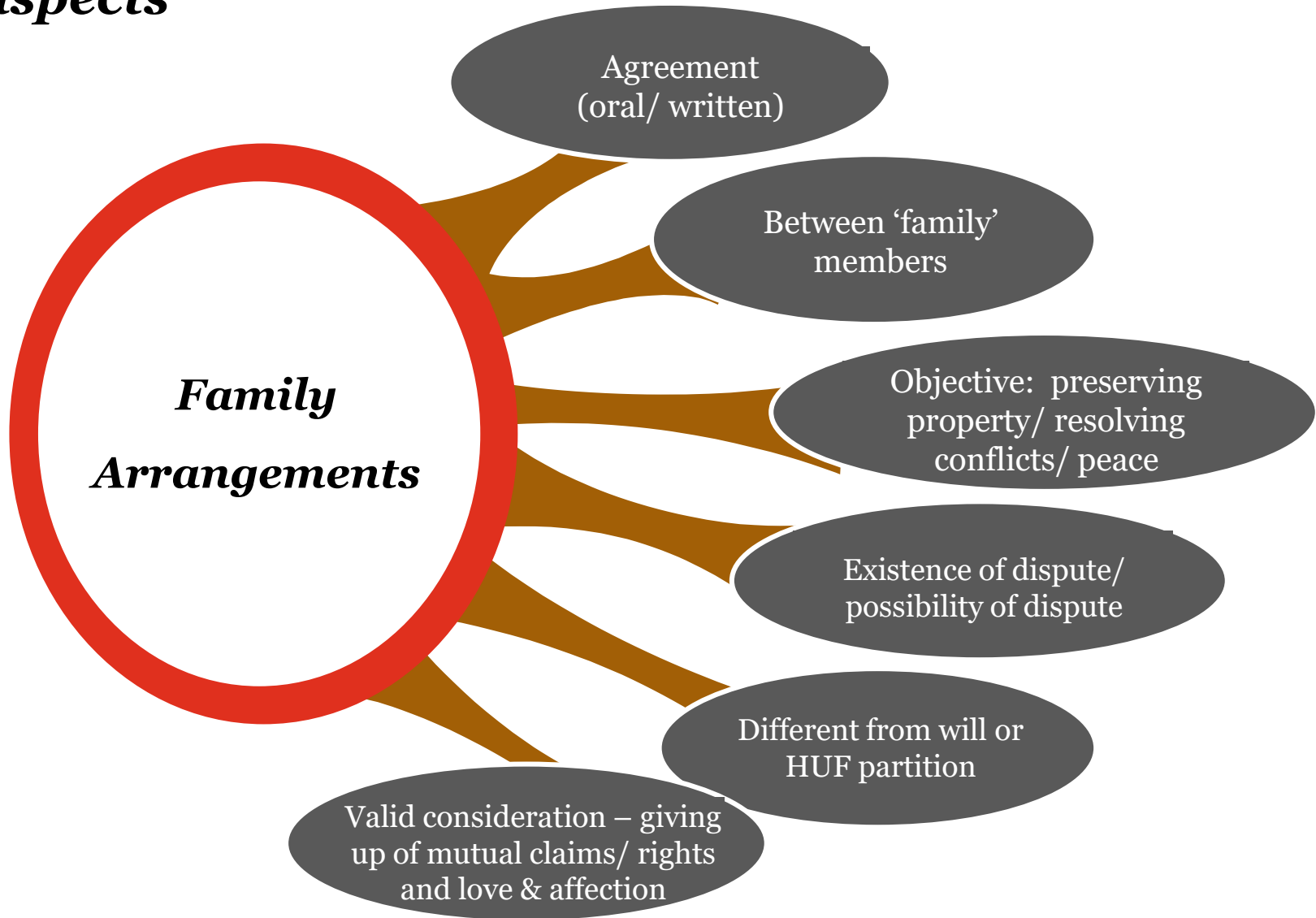


**Shroff
Brothers**

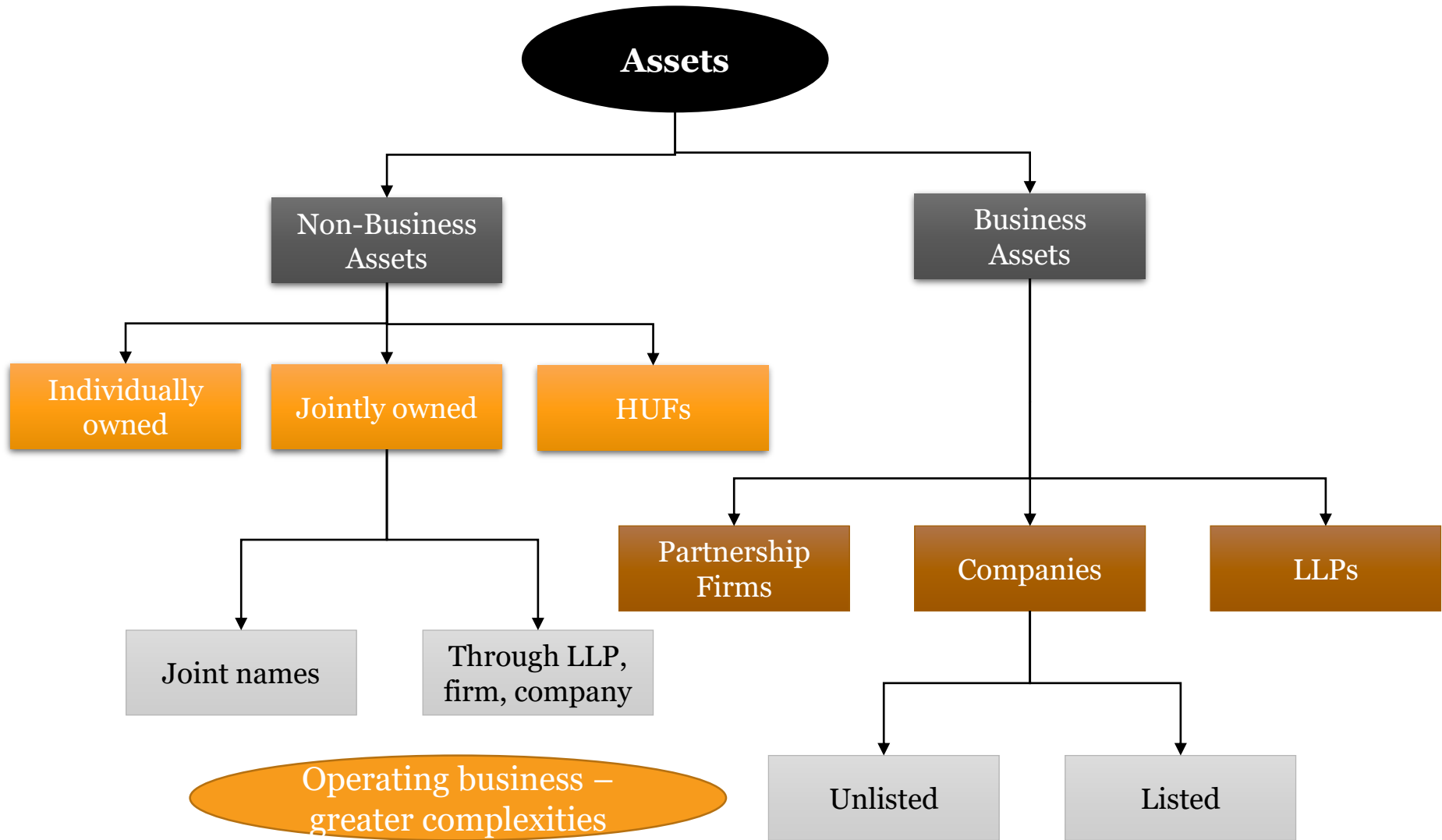
Key aspects of Family Arrangement



Key aspects



Types of assets under Family Arrangement



***Complexities of Family
Arrangement: Commercial,
Regulatory and Tax perspective***



Commercial considerations

'Parties' to the Family Arrangement:

- Members of 'family' ?
- Aligning objectives of each party/ family
- Married daughters ?
- Social aspects (perception of stakeholders, reputation, etc)


'Properties' under Family Arrangement

- Inclusion/ exclusion of assets
- Equitable Settlement versus Equalisation
- Valuation of assets - how ? (date of valuation ?)
- Monetary settlement ?


Other common facets:

- Split of costs (fiscal, legal, consultants etc) and taxes
- Dispute resolution mechanism
- Housing of Common Brands
- Non-compete in business
- Implementation and timelines

Tax issues under the Income Tax Act, 1961 ('ITA')



Capital gains implications in the hands of transferor



Deemed income provision in the hands of recipient (transferee)



Company as a party to Family Arrangement ?



Applicability of GAAR provisions

Tax issues (Capital Gains)

Whether transfer of capital assets in a Family Arrangement is 'transfer' u/s 2(47) of the ITA ?

Transfer of capital assets not a 'transfer'

- Judicial precedents - not a 'transfer', bonafide family arrangement

Meaning of 'family' in a Family Arrangement:

- To be understood in wider sense
- Not only close relations or legal heirs, persons having antecedent title, semblance of claim, etc.

Tax issues (Deemed Income)

Whether capital assets received in family arrangement can be treated as deemed income in the hands of recipient ?

Section 56(2)(x):

- Property received without/ inadequate consideration
- ‘Consideration’ – always in monetary terms ?

In the context of gift tax:

- Judicial precedents, transfer under a family arrangement **is not without consideration**
- Non-monetary consideration
 - prevention of any protracted litigation,
 - preserving the family property,
 - peace and security of the family, etc

Tax issues (Corporate Structuring & GAAR)

Can corporates can be a part of Family Arrangement ?

- Properties held by a common holding company
 - Shares of operating companies
 - Immovable Properties
- Transfer of properties from company in a Family Arrangement - 'transfer' ?
- Judicial Precedents:
 - Company is a separate legal entity
 - Distinct from family members
 - Taxable 'transfer'
- Segregation of properties by way of mergers/ demergers
 - Specific exemption under the ITA, subject to restrictive conditions

Whether GAAR provisions can be attracted ?

Regulatory aspects

Absence of
specific law ?

Absence of specific law

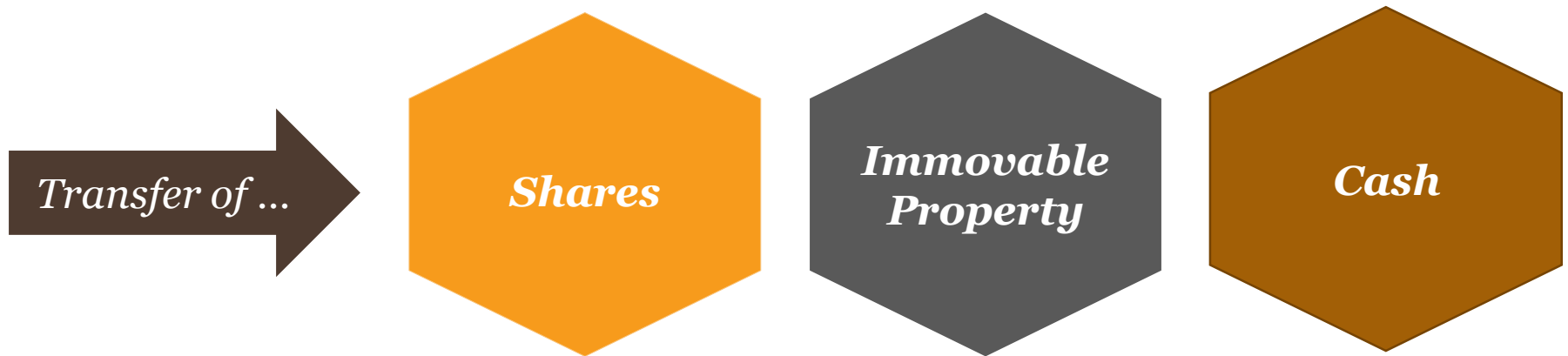
- no specific law on the subject of family arrangement,
- multiple regulations may be involved

Mandatory Registration of 'Deed of Family Arrangement' ?

- *Section 17 of the Registration Act, 1908*
- *Oral Agreement/ Written Agreement ?*
- *Memorandum or Record or Agreement of Transfer ?*

Regulatory aspects (FEMA) ... 1/2

If recipient family member is a non-resident



Whether receipt of property considered as gift ?

Regulatory aspects (FEMA) ... 2/2

Shares

- Allowed with prior approval of RBI and
- Subject to certain conditions
- Eg: up to 5% of share capital, between relatives, less than \$50,000, etc

Immovable Properties

- Immovable property (other than restricted properties) is allowed
- Donor to be 'relative' as per Companies Act, 2013

Cash*

- Only up to \$2,50,000 per financial year under LRS Scheme

**** Whether it could be considered that since entitlement to receive cash is a "legitimate amount due to a NRI" – the repatriation could be upto \$1 Mn?***

Regulatory aspects (SEBI)

SEBI (SAST) Regulations, 2011 ('Takeover Code')

Applicability:

- Transfer of shares/ change of control of listed company

Consequence:

- Open Offer

Exemption:

- Transfer between promoters (3 years)
- Transfer between immediate relatives
- Schemes subject to few conditions

Specific exemption from SEBI for Family Arrangement ?

Fiscal Costs (Stamp Duty)



No express provision under the Indian Stamp Act for levy/
exemption

No specific judgements on Family Arrangement

Entry for 'Agreement' ?

Entry for 'Conveyance' ? (for immovable properties)

Stamp Duty likely to be leviable

Key Takeaways



Family Arrangement has multiple dimensions and needs holistic handling

Social/ Commercial/ Regulatory/Tax – All need to converge

Corporates should not be a part of Family Arrangement

Documentation critical to avoid future disputes/ tax or other exposures

Thank You